



## **REPORT OF THE AUDITOR-GENERAL TO THE NORTH WEST PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE TLOKWE CITY COUNCIL**

### **REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS**

#### **Introduction**

1. I have audited the consolidated and separate financial statements of the Tlokwe City Council set out on pages 166 to 248, which comprise the consolidated and separate statement of financial position as at 30 June 2012, the consolidated and separate statement of financial performance, statement of changes in net assets and the cash flow statement for the year then ended and the notes, comprising a summary of significant accounting policies and other explanatory information.

#### **Accounting officer's responsibility for the consolidated financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these consolidated and separate financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2011 (Act No. 6 of 2011) (DoRA) and for such internal control as the accounting officer determines is necessary to enable the preparation of consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.

#### **Auditor-General's responsibility**

3. My responsibility is to express an opinion on these consolidated and separate financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the *General Notice* issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated and separate financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated and separate financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated and separate financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated and separate financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated and separate financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

## **Opinion**

6. In my opinion, the consolidated and separate financial statements present fairly, in all material respects, the financial position of the Tlokwe City Council as at 30 June 2012, and its financial performance and cash flows for the year then ended in accordance with SA Standards of GRAP and the requirements of the MFMA and the DoRA.

## **Emphasis of matters**

7. I draw attention to the matters below. My opinion is not modified in respect of these matters:

## **Restatement of corresponding figures**

8. As disclosed in note 35 to the consolidated and separate financial statements, the corresponding figures for accumulated surplus, expenditure, inventory, non-current assets held for sale, trade receivables from non-exchange transactions, property, plant and equipment, investment property, long-term receivables and creditors have been restated as a result of errors discovered at, and for the year ended 30 June 2012.

## **Unauthorised, irregular and fruitless and wasteful expenditure**

9. As disclosed in note 37.1 to the consolidated and separate financial statements, unauthorised expenditure of R152 515 522 was incurred in the current year and the unauthorised expenditure in respect of prior years of R83 419 225 has not yet been dealt with in accordance with section 32 of the MFMA.
10. As disclosed in note 37.3 to the consolidated and separate financial statements, irregular expenditure of R142 735 673 was incurred in the current year and irregular expenditure from prior years of R172 810 149 has not yet been dealt with in accordance with section 32 of the MFMA.
11. As disclosed in note 37.2 to the consolidated and separate financial statements, fruitless and wasteful expenditure of R2 823 067 was incurred in the current year and fruitless and wasteful expenditure from prior years of R1 440 792 has not yet been dealt with in accordance with section 32 of the MFMA.

## **Material under spending of the budget**

12. As disclosed in note 47 to the consolidated and separate financial statements, the municipality materially underspent the budget by R47 986 290 (2011: R32 990 479), mainly on general expenses and maintenance, employee related cost and bulk purchases. As a consequence, service delivery was affected negatively.

## **Impairments / Material losses**

13. As disclosed in note 30 and 39.10 to the consolidated and separate financial statements, impairments of R26 413 517 (2011: R17 549 168) and material losses of R10 611 480 (2011: R18 545 894) respectively were incurred as a result of significant impairment of debtors and electricity and water losses.

## **Additional matter**

14. I draw attention to the matter below. My opinion is not modified in respect of this matter:

## **Unaudited supplementary annexures**

15. The supplementary information set out on pages 249 to 267 does not form part of the consolidated and separate financial statements and is presented as additional information. I have not audited these annexures and accordingly I do not express an opinion thereon.

## REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

16. In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

### **Predetermined objectives**

17. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages 23 to 134 of the annual report.
18. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury annual reporting principles and whether the reported performance is consistent with the planned objectives. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury Framework for managing programme performance information (FMPPI).
19. The reliability of the information in respect of the selected objectives is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).
20. The material findings are as follows:

### **Usefulness of information**

21. Section 46 of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) requires the disclosure of measures taken to improve performance in the annual performance report where planned targets were not achieved. Adequate and reliable corroborating evidence could not be provided for all measures taken to improve performance as disclosed in the annual performance report. The municipality's records did not permit the application of alternative audit procedures. Consequently I did not obtain sufficient appropriate audit evidence to satisfy myself as to the validity, accuracy and completeness of the measures taken to improve performance.
22. Section 41(c) of the MSA requires that the integrated development plan should form the basis for the annual report, therefore requiring the consistency of objectives, indicators and targets between planning and reporting documents. A total of 59% of the reported objectives, 65% of the reported indicators and a total of 83% of the reported targets are not consistent with the objectives, indicators and targets as per the approved integrated development plan. This is due to the lack of proper monitoring and control over of the reporting documents by management.
23. The National Treasury FMPPI requires that performance indicators be well defined and verifiable and targets be specific, measureable and time bound:

A total of 45% of the indicators relevant to Community Services, Infrastructure and Housing and planning were not well defined in that clear, unambiguous data definitions were not available to allow for data to be collected consistently.

A total of 60% of the indicators relevant to Community services, Infrastructure and Housing and Planning were not verifiable in that valid processes and systems that produce the information on actual performance did not exist.

A total of 60% of the targets relevant to Community Services, Infrastructure and Housing and Planning were not specific in clearly identifying the nature and the required level of performance.

The required performance could not be measured for a total of 64% of the targets relevant to Community Services, Infrastructure and Housing and Planning

This was due to the fact that management was aware of the requirements of the FMPPI but did not receive the necessary training to enable application of the principles.



## Reliability of information

24. The FMPPI requires that the indicator be accurate enough for its intended use and respond to changes in the level of performance and that documentation addressing the systems and processes for identifying, collecting, collating, verifying and storing information be properly maintained:

A total of 28% of the actual reported target indicators relevant to Infrastructure were not valid, accurate and complete, as for 14% of the indicators the actual reported information did not agree to the source documentation provided while for 14% of the indicators I was unable to obtain sufficient appropriate audit evidence for all the information and explanations I considered necessary to satisfy myself as to the accuracy and completeness.

A total of 74% of the actual reported targets indicators relevant to Community services were not valid, accurate and complete, as for 26% of the indicators the actual reported information did not agree to the source documentation provided while for 48% of the indicators I was unable to obtain sufficient appropriate audit evidence for all the information and explanations I considered necessary to satisfy myself as to the accuracy and completeness.

This was due to limitations placed on the scope of my work by the absence of information systems and processes for identifying, collecting, collating, verifying and storing information.

## Additional matters

25. I draw attention to the following matters below. These matters do not have an impact on the predetermined objectives audit findings reported above.

## Achievement of planned targets

26. Of the total number of planned targets, only 54 targets were achieved during the year under review. This represents 42% of total planned targets that were not achieved during the year under review. This was mainly due to the fact that indicators and targets were not suitably developed during the strategic planning process.

## Compliance with laws and regulations

27. I performed procedures to obtain evidence that the municipality has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the *General Notice* issued in terms of the PAA are as follows:

## Budget

28. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the MFMA.
29. The annual budget of the municipality is not based on the development priorities and objectives as well as the performance targets set by the municipality in its integrated development plan as required by regulation 6 of the Municipal Planning and Performance Management Regulations, 2001.

## Strategic planning and performance management

30. The municipality did not implement a framework that describes and represents how the municipality's cycle and processes of performance planning, monitoring, measurement, review, reporting and improvement will be conducted, organised and managed, including determining the roles of the different role players as required by section 38, 39, 40 and 41 of the MSA read with regulations 7 and 8 of the Municipal Planning and Performance Management Regulations, 2001.

31. The municipality did not afford the local community at least 21 days to comment on the final draft of its integrated development plan before the plan was submitted to council for adoption, as required by regulation 15(3) of the Municipal planning and performance management regulations.
32. The municipality did not give effect to its integrated development plan and conduct its affairs in a manner which was consistent with its integrated development plan, as required by section 36 of the MSA and Municipal planning and performance management regulation 6.
33. The municipality did not set appropriate key performance indicators as a yardstick for measuring performance, including outcomes and impact, with regard to the municipality's development priorities and objectives set out in its integrated development plan or set measurable performance targets with regard to each development priority and objective as required by section 41 of the MSA.
34. The accounting officer of the municipality did not by 25 January assess the performance of the municipality during the first half of the financial year, taking into account the municipality's service delivery performance during the first half of the financial year and the service delivery targets and performance indicators set in the service delivery and budget implementation plan as required by section 72(1)(a)(ii) of the MFMA.

### **Procurement and contract management**

35. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by Supply chain management (SCM) regulation 17(a) and (c).
36. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a).
37. Invitations for competitive bidding were not always advertised for a required minimum period of days, as required by SCM regulation 22(1) and 22(2).
38. The preference point system was not applied in all procurement of goods and services above R30 000 as required by section 2(a) of the Preferential Procurement Policy Framework Act, 2000 (Act No. 5 of 2000) (PPPFA) and SCM regulation 28(1)(a).
39. Contracts were awarded to bidders based on preference points that were not allocated and calculated in accordance with the requirements of the PPPFA and its regulations.
40. Contracts were awarded to providers whose tax matters had not been declared by the South African Revenue Service to be in order, as required by SCM regulation 43.
41. Awards were made to providers who are persons in service of other state institutions or whose directors/ principal shareholders are persons in service of other state institutions, in contravention of SCM regulations 44. Similar awards were identified in the prior year and no effective steps were taken to prevent or combat the abuse of the SCM process in accordance with SCM regulation 38(1).
42. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM regulation 46(2)(e)/ the code of conduct for councillors issued in terms of the MSA/ the code of conduct for staff members issued in terms of the MSA.
43. Persons in service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM regulation 46(2)(e)/ the code of conduct for councillors issued in terms of the MSA/ the code of conduct for staff members issued in terms of the MSA.
44. The prospective providers list for procuring goods and services through quotations was not updated at least quarterly to include new suppliers that qualify for listing, and prospective providers were not invited to apply for such listing at least once a year as per the requirements of SCM regulation 14(1)(a)(ii) and 14(2).



45. Construction contracts were awarded to contractors that were not registered with the Construction Industry Development Board (CIDB) and/or did not qualify for the contract, in accordance with section 18(1) of the CIDB Act, 2000 (Act No. 38 of 2000) and CIDB regulations 17 and 25(7A).
46. Contracts were awarded to bidders that did not score the highest points in the evaluation process, as required by section 2(1)(f) of the PPPFA.

#### **Annual financial statements and annual performance report**

47. The financial statements submitted for audit were not in all material respects prepared in accordance with the requirements of section 122 of the MFMA. Material misstatements of cash and cash equivalents, creditors and trade receivables identified by the auditors were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.
48. The 2010/11 annual report was not tabled in the municipal council within seven months after the end of the financial year, as required by section 127(2) of the MFMA.
49. The municipal council did not adopt an oversight report, containing comments on the annual report, within two months from the date on which the 2010/11 annual report was tabled, as required by section 129(1) of the MFMA.
50. The annual performance report for the year under review does not include a comparison of the performance with the previous financial year development priorities, objectives and performance indicators set out in its integrated development plan, as required by section 46(1)(b) of the MSA.

#### **Internal audit**

51. The internal audit did not audit the results of performance measurements, as required by section 45(1)(a) of the MSA and Municipal Planning and Performance Management Regulation 14(1)(a).
52. The internal audit unit did not assess the functionality of the performance management system, whether the performance management system complied with the requirements of the MSA and the extent to which the performance measurements were reliable in measuring the performance of the municipality on key and general performance indicators, as required by Municipal Planning and Performance Management Regulation 14(1)(b) (i),(ii),(iii).
53. The internal audit unit did not audit the performance measurements on a continuous basis, as required by Municipal Planning and Performance Management Regulation 14(1)(c).

#### **Expenditure management**

54. The accounting officer did not take effective steps to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.
55. Unauthorised, irregular, fruitless and wasteful expenditure was not recovered from the liable person, as required by section 32(2) of the MFMA.

#### **Human resource management**

56. The competencies of financial and supply chain management officials were not assessed promptly in order to identify and address gaps in competency levels as required by the Municipal Regulations on Minimum Competency Levels regulation 13.
57. The municipality did not submit a report on compliance with prescribed competency levels to the National Treasury and relevant provincial treasury as required by the Regulations on Minimum Competency Levels regulation 14(2)(a).
58. The annual report of the municipality did not reflect information on compliance with prescribed minimum competencies as required by the Regulations on Minimum Competency Levels regulation 14(2)(b).

## **Waste management**

59. The municipality's operational activities on their waste disposal site contravened or failed to comply with the requirements of a waste management license or permit and the norms and standards in terms of section 67(1)(f) and (h) of the National Environmental Management: Waste Act, 2008 (Act No. 59 of 2008) (NEMWA) and section 29(4) of the Environmental Conservation Act, 1989 (Act No. 73 of 1989).
60. The municipality's waste management and disposal activities contravened or failed to comply with the requirements of section 28(1) of the National Environmental Management Act, 1998 (Act No. 107 of 1998) and sections 16(1)(c) and (d) and 26(1)(b) of the NEMWA.

## **Moorivier Mall Investment Company Limited (MMIC)**

61. Section 86E(1)(a) of the MSA allows that a municipality may establish a company only for the purpose of utilising the company as a mechanism to assist in the performance of any of its functions and powers. Contrary to this requirement, the municipality established and exercised effective control over the MMIC which assists the community in obtaining shares in the recently developed Moorivier Mall. As reported in the prior year it is recommended that the municipality release its effective control through the appointment of directors which are not councillors of the municipality.

## **Internal control**

62. I considered internal control relevant to my audit, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters reported below are limited to the significant deficiencies that resulted in the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

## **Leadership**

63. Management failed to timely appoint sufficient appropriately skilled staff in key positions within the finance, performance reporting and supply chain management units, furthermore the training and development initiatives failed to address the underlying deficiencies that caused non compliance and predetermined objective matters to be repeatedly reported on in the audit report. Policies and procedures did not adequately guide performance activities and compliance with laws and regulations.

## **Financial and performance management**

64. The municipality did not implement a proper record keeping system to ensure that complete, relevant and accurate information is accessible and available to support performance reporting and compliance with laws and regulations. Management's internal controls and processes over the preparation and presentation of financial statements were not able to ensure that the financials were free from material misstatements resulting in material corrections that had to be made during the audit.

## **Governance**

65. Management failed to implement appropriate risk management activities to ensure that regular risk assessments are conducted and that a risk strategy is developed and monitored to address the risks.
66. The internal audit department was not effective during the financial year. Council and management failed to recognise the value that internal audit can add to the municipality.

67. The audit committee fulfilled its function, however the municipality did not adequately respond to the concerns raised, resulting in the internal control environment over performance reporting and compliance with laws and regulations being ineffective.

Auditor General

Potchefstroom

30 November 2012



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*